No. 8881

In the United States Circuit Court of Appeals

For the Ninth Circuit

INVESTORS SYNDICATE, PORTLAND TRUST AND SAVINGS BANK, Trustee, and METROPOLITAN LIFE INSURANCE COMPANY,
Appellants.

vs.

LLOYD R. SMITH, Trustee in the Matter of Guaranty Trust Company, a corporation, and National Investment Company, a corporation, its affiliate, Bankrupts, GESINA KING, HELEN WINSOR JOHNSON, BERT WHY and ELSA STRATHMAN, MRS. GOW WHY, CONRAD BAURIEDEL, IDA ISABELL NEILSON, GEORGE J. and EMMA C. FOURIER, JAMES T. JONES and LOUIS KNUTSON, and RALPH A. COAN and S. J. BISCHOFF,
Appellees.

APPELLANTS' REPLY BRIEF

Upon Appeal from the District Court of the United States for the District of Oregon.

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STATEMENT OF THE CASE

In an effort to explain away the segregation order signed by Judge McNary at the outset of the

proceedings after the hearing before the Special Master, appellees claim that the order "deals with bookkeeping only" and was not made on petition of the appellants. The fact is appellants appeared at the first meeting of creditors and opposed continuance of the bankrupt in possession (R. 6), and it was on account of what transpired at the original and adjourned hearing before the Special Master that the latter recommended to the court that a separate account be kept of all moneys coming into the Trustee's hands.

Section 47 (A) 6 of the Bankruptcy Statute requires the Trustee "to keep regular accounts showing all amounts received and from what sources and all amounts expended and on what account". See also General Order Number XVII. It was therefore not necessary for the court to enter an order requiring the Trustee to keep itemized accounts, because the statute already required this. The purpose of the order was to segregate the collections and expenses as to the various mortgaged properties.

Again, appellees are in error in stating that the court's order of segregation did not apply exclusively to the mortgaged properties. Not only is it true that the court had the mortgaged properties in mind, as is shown by consideration of the Special Master's report, but it is further an admitted fact in this case, referring to income exclusively from the mortgaged properties, that **such income was practically all the income that the two debtor cor-**

porations had; that during the administration of the Trustee in the bankruptcy proceedings the debtors were in a state of collapse, having virtually no income except from the mortgaged properties" (R. 69). Since the debtor, both before and after bankruptcy, had virtually no income except from the mortgaged properties, the order referring to segregation of income obviously could refer only to the mortgaged properties.

ASSIGNMENTS OF ERROR ARE SUFFICIENT

The appellees contend (Br. pp. 5 to 7) that the assignments of error are insufficient in that they fail to point out whether the error lies in lack or insufficiency of evidence to support the ruling of the Court or the erroneous conception or application of legal principles. They cite and rely upon cases from the Ninth Circuit in which it has been held that certain assignments of error are insufficient as being too general. The authorities do not sustain appellee's contention.

The authorities hold that an assignment of error must point out the particular act of the court which is alleged to be erroneous: *Am. Surety Co. vs. Fisher Warehouse Co.* (9 C.C.A.), 88 Fed. (2d) 536. The authorities do not hold that the assignment of error must contain legal reasons supporting appellant's contention. *Randolph vs. Allen* (5th C.C.A.), 93

Fed. 23; *A. T. & S. F. R. Co. vs. Meyers*, (7th C.C.A.), 76 Fed. 443. An appellant is not required to speculate as to what caused the judicial mind to reach an erroneous legal conclusion. Assignments that court erred in denying defendant's motion for a directed verdict (*A. T. & S. F. R. Co. vs. Meyers, supra; Kennedy Lumber Co. vs. Rickborn* (4. C.C. A.), 40 Fed. (2d) 228); that court erred in sustaining demurrer to complaint (*Smith vs. Royal Ins. Co.* (9th C.C.A.), 93 Fed. (2d) 143), that court erred (1) in overruling demurrer to complaint, and (2) in denying motion for directed verdict (*Southern Pac. Co. vs. Swartz* (9th C.C.A.), 89 Fed. (2d) 192), have been held to be sufficient under the rule. Also it was held in *Gartner vs. Hays* (8th C.C.A.), 272 Fed. 896, that a specification that court erred in its conclusions of law is sufficient to raise the question of whether the court's findings of fact are sufficient to sustain its legal conclusions.

The only question involved in this appeal is the correctness of the conclusion of law. There is presented for consideration no question of proceedings at the trial and no question of fact. The facts found by the Special Master were not excepted to and so stand as admitted. Furthermore, the facts have been stipulated on appeal under Equity Rule 77. The facts being admitted, the sole question is whether those facts entitle the mortgagees to the rents. The Special Master concluded that they did, but the trial court, being of the opposite opinion, sustained ex-

ception to the legal conclusions of the Special Master. The question is, did the court err in so doing.

Nor do the assignments of error violate the rule that each error relied upon must be separately assigned. There were separate assignments of error for each of the three appellants, directed to the Special Master's conclusions affecting the properties upon which each held a mortgage. The first assignment on behalf of Investors Syndicate covers the first five conclusions of law of the Special Master, which relate to the five apartment houses owned by Investors Syndicate. Since the question of law as to each of said apartment houses is identical, there was really involved only one question of law, namely, whether Investors Syndicate is entitled to recover the rentals from its mortgaged properties. To have specified error separately as to each apartment house would have been useless repetition. The same is true as to assignment No. 3 made on behalf of Portland Trust and Savings Bank, and covering conclusions of law six and seven which related to the two mortgaged premises of the Portland Trust and Savings Bank, as to each of which the same legal question was presented.

As counsel for appellees have pointed out there is really only one assignment of error in the case as to each of the appellants. The second assignment as to each mortgagee is the converse of the first. The error assigned is the act of the court in sustaining exceptions to the conclusions of law in the report of

the Special Master. The error complained of is thus specifically pointed out. Since that error is in making a conclusion of law, to specify *why* it was erroneous would trench upon the function of the brief and so incumber the record, as pointed out in the cases previously cited. The assignments do point out specific rulings of the trial court which are alleged to be erroneous, and so present the question whether, based upon the admitted facts, the appellants are or are not as a matter of law entitled to the rents.

We submit that the assignments of error are sufficient to raise the sole question involved in this appeal under a strict interpretation of the rules. But since assignments of error are abolished altogether under the new rules governing appeals, it would seem reasonable that the old rules as to the few cases to which they are still applicable should be applied with some degree of liberality, especially where the issue on appeal is a single question of law.

INTERVENTION OF BANKRUPTCY PRIOR TO RECEIVERSHIP DOES NOT BAR MORTGAGEE'S ORDINARY REMEDIES OR THEIR EQUIVALENT.

Appellees labor to show that assignment of rents is a mere contract for a future lien which, not being perfected at the time of bankruptcy, entirely fails. In an effort to support this argument, which is entirely unsupported either in reason or authority, appellees claim that the bankruptcy cases award-

ing rents and profits to the mortgagee after bankruptcy, in the absence of receivership proceedings prior to bankruptcy, arise solely in jurisdictions where the common law theory of mortgages prevails. This argument is fallacious throughout.

MORTGAGEE'S CLAIM TO RENTS PRESENTS QUESTION SOLELY OF REMEDY.

The fallacy of counsel's argument concerning so-called failure to perfect lien prior to bankruptcy in a case where the mortgagee does nothing until bankruptcy, lies in the failure to distinguish between the lien right and the lien remedy. Application of rents and profits is a matter of remedy which flows as part of the original mortgage lien, where the mortgage contains appropriate provisions as in the present case. In the absence of voluntary surrender of possession, the rents are ordinarily obtained by application for a receivership, but when bankruptcy supervenes, a receiver cannot be appointed, as the bankruptcy court has sole jurisdiction. Therefore, the bankruptcy court gives an equivalent remedy suitable to the bankruptcy procedure. That is the reasoning of the courts in the many cases which we have cited in our main brief. (See Appellants' Brief, pp. 25, 28.)

The right to the rent remedy is determined by the validity of the mortgage itself, it being admitted in this case that the mortgage was for valuable consideration and was duly recorded and entitled

to the protection of Sec. 67D of the Bankruptcy Act (R. 27, 60). It might just as well be argued that the mortgage lien on the land itself is inchoate, as to argue that the remedy of application of the rents and profits is an inchoate lien right. In both cases all the mortgagee has is a lien, remedy on which is postponed until default, at which time the mortgagor must bring suit to foreclose before he can realize on his lien on the land, and must, in the absence of bankruptcy, ask for a receiver in order to obtain the rents and profits. After bankruptcy, foreclosure proceedings cannot be instituted without the bankruptcy court's consent and even thereafter the bankruptcy court may, if it wishes, retain possession until the bankruptcy proceedings are completed. But such possession from and after the date of the application by the mortgagee for the rents and profits is subject to application of those rents and profits to the mortgagee's account. We said in our original brief, and we repeat it now, that all of the cases so hold, the only difference being that some of the cases go even further and state that when the application is filed the mortgagee is entitled retroactively to the date of the institution of the bankruptcy proceedings. We challenged counsel to find one case to the contrary. That challenge has not been met.

It is no answer for counsel to state (Appellees' Brief, p.19), "There is in Oregon no substitute for this method of taking possession" (to-wit, the re-

ceivership method described by the Oregon statute). Neither Oregon nor any other state has or could attempt to legislate as to what remedies will be allowed in a court of bankruptcy. Section 67D of the Bankruptcy Act protects the mortgage lien, which includes all the mortgage incidents attendant to and flowing from the mortgage itself, such as the right to the rents and profits.

As said by the Supreme Court:

> "The bankruptcy act did not attempt, by any of its provisions, to deprive a lienor of any remedy which the law of the State vested him with." Hiscock v. Bank, 206 U.S. 28, 41, 51 L. ed. 945, 953.

Cases which deny the validity of a lien which was not perfected prior to bankruptcy, such as an unrecorded mortgage or conditional sales contract, are, of course, entirely out of point because they are not entitled to the protection of Section 67D of the Bankruptcy Act.

BANKRUPTCY COURTS GRANT SEQUESTRATION WHETHER MORTGAGE CONTROLLED BY COMMON LAW OR LIEN THEORY.

We turn now to consideration of appellees' statement that all of the cases cited by us in our main brief are from so-called common law jurisdictions rather than lien jurisdictions.

Our first answer is that we cited cases of mortgages in a number of jurisdictions where the lien theory rather than the common law theory of mort-

gages prevails, to-wit:

CALIFORNIA:

American Trust Co. v. England, 84 F. (2d) 352 (C.C.A. 9).
Re Hotel St. James Co., 65 F. (2d) 82 (C.C. A. 9).

NEW YORK:

In re. Brose, 254 F. 664.
Prudential Insurance Co. v. Liberdar, 74 F. (2d) 50 (C.C.A. 2).
Lincoln Bank v. Realty Associates, 67 F. (2d) 895.

WISCONSIN:

Re Clark Realty Co., 234 F. 576 (C.C.A. 7).

FLORIDA:

Florida Bank v. U. S., 87 F. (2d) 896 (C.C.A. 5).

Appellees' brief (appendix) contains a digest of the laws of various states on this point, but it will be noticed that none of the states above mentioned is included in this appendix, indicating that counsel concedes that these cases arose in jurisdictions adhering to the lien theory of mortgages, just as Oregon does. The same authority cited by counsel, to-wit, 1 Jones, Mortgages, 8th ed., bears out the fact that the above states subscribe to the lien theory. See Sections 67, 22, 26, 48, 65.

It will further be noticed that although counsel argues extensively that Florida adheres to the common law theory, the appendix makes no reference to the law of Florida. Counsel argues that in Florida

a deed of trust, as distinguished from an ordinary mortgage, passes legal title and the right to possession, citing *Sautter v. Miller,* 15 Fla. 625. (See Appellees' Brief, p. 32.) The fact is that in Florida **all mortgages** give a mere lien to the mortgagee. Section 5725 of 1927 Compiled Laws of Florida, provides:

> "A mortgage shall be held to be a specific lien on the property therein described and not a conveyance of the legal title or of the right of possession."

This statute was enacted in 1853. It is, accordingly, held in Florida that the mortgagor is not entitled to possession until after foreclosure and sale: *Pasco v. Gamble,* 15 Fla. 562; *White Engineering Corp. v. Bank,* 81 Fla. 35, 87 So. 753. The mortgagor retains the rents: *Endall v. Walls,* 16 Fla. 786. This section was construed as abrogating the common law rule: *Walker v. Huge,* 78 Fla. 667, 83 So. 605; *Evins v. Bank,* 80 Fla. 84, 85 So. 869.

There is nothing in the Florida law making any distinction as to a mortgage in the form of a deed of trust. The case relied on by counsel of *Sautter v. Miller, supra,* was decided on the express ground that the trust deed in that case was for general trust purposes, and was no mortgage at all.

Appellees in an effort to distinguish the *Livingston* case, contend that Missouri is a common law jurisdiction, but neglect to mention that 1 Jones, Mortgages, 8th ed., Sec. 67, classifies Missouri as neither a common law nor a lien state, stating that

Missouri modifies the common law in that until breach of condition and possession taken the mortgagor is regarded as owner, even against the mortgagee.

The remaining states which Jones classifies as common law jurisdictions are Alabama, Illinois, Massachusetts, New Jersey, Ohio and Pennsylvania. It therefore appears that we have cited cases from five jurisdictions that are common law jurisdictions, four jurisdictions that are lien states, and one state that has a hybrid rule of mortgage law. How, under these facts, can counsel contend, as stated at page 41 of Appellees' Brief, that "the element common to all the cases cited by appellants is that in all of the states in which the mortgages were made, the mortgagee by virtue of the mortgage and the law of the state applicable thereto had the legal title, the immediate right of possession, and the immediate right to the rents."

Again, in answer to appellees' contention based on whether the particular state has a common law or lien theory, it should be noted that in not one of the cases cited by us was any such distinction raised or even suggested. On the contrary, all these cases held strictly as a matter of bankruptcy law that remedies which were open to the mortgagee in absence of bankruptcy should not be denied subsequent to bankruptcy, and that therefore the bankruptcy court would supply an equivalent remedy. We quote again from *Bindseil v. Liberty Trust Co.*,

248 F. 112 (C.C.A. 3):

> "This view is not based upon the notion that the mortgage confers a lien on rents, for, of course, it does not; but it is based upon what is conceived to be an equitable adjustment of rights, of which some are obviously superior to others. Such an application of income from encumbered property appears to be not only an equitable but a very practical way of administering bankrupt assets."

NO REASON FOR ANY DISTINCTION BETWEEN COMMON LAW AND LIEN STATES

There is no logical reason for any distinction between the common law states and the lien states. In all jurisdictions, even where the common law theory prevails, the mortgagor is not entitled to the rents and profits until he obtains possession or has a receiver appointed: 2 Jones, Mortgages, 8th ed., Sec. 976. See *Elmore v. Symonds,* 183 Mass. 321, 67 N.E. 314; *Meyers v. Brown,* 92 N.J. Eq. 348, 112 Atl. 844. We call the court's attention to the fact that in all the states subscribing to the common law theory, an ejectment action is necessary before the mortgagee can obtain possession and have the rents. See Appellees' Brief, Appendix, pp. 1-5.

If a mortgagee in a common law state has not yet obtained possession by an action in ejectment, he is in precisely the same position as a mortgagee in a lien state who has not obtained the appointment of a receiver prior to bankruptcy. In both

cases the mortgagee has a remedy which has not been exercised as of the date of bankruptcy. In both cases the bankruptcy court, being a court of equity, will supply a remedy equivalent to the state court remedy.

The Supreme Court has stated (referring to 77B proceedings):

> "They are essentially courts of equity and their proceedings inherently proceedings in equity * * *." *Continental Illinois Bank v. R. R.*, 294 U.S. 648, 675, 79 L. Ed. 1110, 1128.

The *Continental Illinois Bank case,* far from supporting appellees' theory, well illustrates the fallacy of confusing a property right with a remedy. In that case the court, under Section 77 of the Bankruptcy Act, restrained the sale of collateral held by a mortgagee in possession. In reaching that result the court gave careful consideration to Section 67D of the Bankruptcy Act and held that the injunction did not infringe, because (294 U.S. at 676):

> "The injunction here in no way impairs the lien * * * it does no more than suspend the enforcement of the lien * * *."

ADDITIONAL REASONS TO PROTECT MORTGAGEE UNDER SECTION 77B.

In our main brief (pp. 35-39), we considered the mortgagee's rights under 77B and pointed to the widened scope of 77B proceedings and especially the

fact that in addition to the ordinary powers granted under the Bankruptcy Act, Section 77B endows the court with all the powers of a Federal court in a general equity receivership. We further showed that every case in which the point has arisen under 77B, was decided in favor of the mortgagee.

Appellees concede that under the case of *Prudential Insurance Co. v. Liberdar*, 74 F. (2d) 50 (C.C.A. 2), the Federal Court in a general equity receivership will award the rents and profits to the mortgagee from and after the date of application therefor (Appellees' Br. p. 40). But appellees claim that because this is a bankruptcy proceeding the *Liberdar* case is of no authority.

Our answer to this is that Section 77B (a) gives to the court all of the powers that the Federal Court had in a general equity receivership such as the *Liberdar* case: *Duparquet v. Evans*, 297 U.S. 216, 80 L. ed. 591.

Since we are considering the jurisdiction of the court, and not the powers of the trustee, counsel's references to the latter are irrelevant. However, if counsel had fully quoted Section 77B(c)(2) instead of breaking off the quotation, it will be noted that same reads as follows (words omitted by counsel are underlined):

> "Every such trustee upon filing such bond, shall have all the title and shall exercise, subject to the control of the judge and consistently with the provisions of this section, all the powers

> of a trustee appointed pursuant to Section 44 of this Act, *and if authorized by the judge, the same powers as those exercised by a receiver in equity to the extent consistent with this section* * * *."

Appellees further contend, p. 56, that the power under 77B to restrain pending foreclosure proceedings existed under ordinary bankruptcy. The contrary has been conclusively determined in many decisions. See, for example: *Straton vs. New,* 283 U. S. 318; 75 L. ed. 1060. *Hiscock vs. Bank,* 206 U.S. 28; 51 L. ed. 945. *Metcalf Bros. vs. Barker,* 187 U.S. 165; 47 L. ed. 122. It is useless for counsel to contend that 77B did not greatly amplify the powers of the bankruptcy court, thereby imposing upon it the duty to protect the remedy of the lienor by supplying an equivalent of what the lienor would have had in the absence of 77B proceedings.

We submit that counsel have failed entirely to answer our point with reference to 77B and we call the court's attention to the fact that no cases are cited by counsel under 77B where the mortgagee was barred after filing application for the rents.

NAYBERGER CASES NOT IN POINT

Counsel cite *State ex rel Nayberger v. McDonald,* 128 Or. 684, 274 P. 1104, and *McKinney v. Nayberger,* 138 Or. 203, 6 P. (2d) 228. These cases are entirely out of point. They are cited in support of counsel's contention concerning the Oregon law

relating to mortgages. But in the Nayberger cases the mortgagee held a second mortgage which contained no provision for application of the rents and profits. Since the rents and profits were not pledged as permitted by Section 5-112 of the Oregon Code, the trial court order appointing the receiver was void. The mortgagee in that case was a second mortgagee, the first mortgagee not being a party to the suit. The first mortgage contained appropriate provisions for application of rents, but it was held that there were no grounds whereunder the second mortgagee could claim subrogation and therefore the mortgagee could not benefit by the provisions of the first mortgage.

SPECIAL FACTS RELATING TO PORTLAND TRUST AND SAVINGS BANK.

Our main brief, pp. 46, 47-56, showed that Portland Trust & Savings Bank's remedy was exercised prior to bankruptcy and that the rentals were impounded in the state court not only before bankruptcy but after institution of bankruptcy proceedings and until the filing of 77B proceedings. It is not true, as appellees claim, that there was anything informal about the treatment throughout these proceedings of Portland Trust's claim as being on a trust basis in recognition of its rights to the rents and profits, because we have already shown that the bankruptcy court itself issued an order permitting the trustee in bankruptcy before

77B proceedings to pay the moneys to the state court in the foreclosure proceedings of Portland Trust (R. 11-12). When 77B proceedings were instituted they had the effect of staying the state court proceedings so that from that time the rents were collected by the bankruptcy court.

Under the case of *Hitz v. Jenks,* 123 U.S. 297, payment of the rentals into the court by the mortgagor, acting under court order, was the equivalent of a court receivership. The discussion of appellees (p. 65) is in no way to the contrary. The court in the *Hitz* case required the plaintiff to collect the rents and pay them into court, and as to all rents subsequently collected, although the order was not denominated a receivership order, it was held that the procedure was equivalent to a receivership. The identical situation is true in our case, except that the party appointed to collect the rents and pay them into court was the defendant instead of the plaintiff. The rents were just as effectively sequestered as if a third party had been appointed as receiver. By the express order of the state court, the rents when collected were to be applied to the bank's mortgage indebtedness (R. 10).

It is not true that Judge McNary's order, permitting the payments to the state court to continue after bankruptcy proceedings, was set aside as soon as the trustee found out about it and raised the question. On the contrary, the original order was entered by Judge McNary after a motion had been

filed supported by affidavit (R. 11). The trustee raised no further question about the matter until 77B proceedings were instituted, and then for the first time did payments to the state court cease, although even after that time the bankruptcy court, for a period, permitted the rents to be collected by one Kaste.

On these facts it is plain that when the trustee put the Portland Trust funds in a separate bank account and kept them there ever since, the trustee was acting consistently with the bank's rights as recognized by the previous court order.

REPLY TO APPELLEES' CONTENTION THAT 1927 AMENDMENT TO SECTION 5-111, OREGON CODE, IS NOT APPLICABLE TO INVESTORS SYNDICATE MORTGAGES WHICH WERE PREVIOUSLY EXECUTED.

Appellees cite (Br. p. 72) Michigan cases construing an Act of that State of 1925, as supporting their contention that the amendment of 1927 in Oregon cannot be applied to mortgages previously executed. The Michigan Statute of 1925 is of no aid to us in this controversy because of essential differences in wording. The Michigan Statute starts out with the word "hereafter", and this was emphasized in *Newsbaum vs. Shapiro* (Mich.), 228 N.W. 785, as requiring that it be applied only to mortgages subsequently executed. When the difference in language of the statute is considered, the Michigan au-

thorities really support the construction and application for which we contend.

ASCERTAINMENT OF DEFICIENCY

It is contended that the mortgagees have the burden to prove that they bid a fair price at the foreclosure sale and that the bankruptcy court may determine that the actual value was in excess of such amount. This point has no place in the present litigation, because the amount of recovery to be awarded to appellants is a matter for future accounting. This court has before it only the broad legal question as to whether the mortgagee is entitled to rents and profits after application therefor in the bankruptcy court.

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APPENDIX

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Limitation of space makes it impossible in the main reply brief to consider all of the cases cited by counsel. A number of these cases are cited on collateral points or are obviously distinguishable and need not be considered herein. Practically all the cases dealing with the main issue before us are treated in our main brief. It is our belief that in important regards counsel's argument concerning some of these cases is misleading and inaccurate. We feel, therefore, that it will be of assistance to the court in this appendix to consider in alphabetical order certain of these cases, as follows:

American Trust Company v. England, 84 F. (2d) 352 (C.C.A. 9). See Appellants' Brief, pp. 18, 19, 21, 23, 63, 64, 65. Appellee's attempted distinction fails. The trustee in bankruptcy of a third mortgagee was in possession under the latter's mortgage, without the mortgagor's consent. In effect, therefore, the trustee in bankruptcy of the third mortgagee was an assignee of the mortgagor. The mortgagor at no time consented to possession by or for the benefit of the first mortgagee. Nevertheless, the first mortgagee was held to be entitled to the rents from and after date of application in the bankruptcy proceeding of the third mortgagee. The third mortgagee was just as much an adverse party as far as the first mortgagee was concerned as was the owner. The owner was in no way estopped from assert-

ing his position against the first mortgagee, as possession had never been surrendered to the first mortgagee. This court used the following broad language in concluding its decision in the *England* case:

> "This is a proceeding in equity, and we find funds in the possession of the trustee in bankruptcy to which the appellant made proper claim and is in a position equivalent to his possession of the property as mortgagee in possession. Before distribution of the funds, the mortgagor became a party to the bankruptcy proceedings in which the funds are so held. It has had full opportunity as such party to protect its rights. The issue as to the right to the funds should be determined by this court sitting in equity."

The England case is important not only as establishing the mortgagee's rights against the owner, but also as establishing the first mortgagee's rights against the third mortgagee in the bankruptcy proceedings. Since the third mortgagee was in effect an assignee of the mortgagor, the third mortgagee being in possession had the same rights as the mortgagor had against the first mortgagee. Consequently when the bankruptcy court permitted the first mortgagee upon application to obtain the rents and profits, it is clear that the same result would have followed had the bankruptcy been that of the mortgagor instead of that of the third mortgagee.

Bindseil v. Liberty Trust Co., 248 F. 112. Appellees' quotation from the *Bindseil* case (Brief, p. 51) is highly misleading. The paragraph there quoted is

stated by the court as setting forth contentions with which the court disagrees, and the balance of the opinion is devoted to showing why the quoted statement is wrong. The very next words of the court after the portion quoted are as follows:

> "In these decisions the fact of bankruptcy is noted but its effect on the relative rights of creditors is disregarded."

The decisions mentioned are lower court decisions which are distinguishable on their facts.

Continental Illinois Bank vs. Chicago, etc. Company, 294 U.S. 648, 79 L. ed. 1110. It is to be noted that that was a 77B case which merely exemplifies that under 77B the court has the power to do what it does not have the power to do under the ordinary bankruptcy statute, to-wit, restrain a pledgee in possession from foreclosing by sale. Such restraint, of course, is for the protection of the bankruptcy court and subject to the obligation of the court not to impair the lien, but on the contrary to preserve the lienor's rights subject to such delay as is required by the 77B proceedings. As applied to a case of mortgages on income producing real property, the court in 77B may well restrain the enforcement of a mortgagee's remedy even where there was a receivership prior to bankruptcy, but if reorganization fails and the mortgagee is not otherwise protected, the bankruptcy court must provide a retroactive remedy commensurate with the remedy which was stayed. Likewise, if the mortgagee has made no ap-

plication prior to bankruptcy, he is entitled to the same protection from and after the date of application to the bankruptcy court.

Dallas Trust & Savings Bank v. Ledbetter, 36 F. 221 (C.C.A. 5), (Re. Thomas). This case is distinguishable on the same grounds as the St. James case. See Appellants' Brief, p. 29, where the case is discussed under the name of Re Thomas. The quarterly rent came due and was collected April 1st, and the court says that no application was made to the bankruptcy court until "after April 1st". Mortgagee contended sale and foreclosure would have occurred. except for bankruptcy, before April 1st, but that was held to be immaterial. The case is no authority for what would have happened had the application been for rents subsequently collected.

Florida Bank v. U. S., 87 F. (2d) 896 (C.C.A. 5). See supra, pp. 10-11; see also Appellants' Brief, pp. 28, 38. The case is direct authority that the mortgagee is entitled upon application. There is not one word in the opinion bearing out appellees' statement to the effect that the mortgagee was in possession before bankruptcy. See Appellees' Brief, pp. 32-3.

Re Foster, 9 Fed. Cas., p. 523; s.c. on appeal, 9 Fed. Cas., p. 572. This case arose under the Bankruptcy Act of 1867. Furthermore, the case is distinguishable because it was held that the mortgagee was not entitled to rents collected by the bankruptcy court **before** application therefor.

In re Hotel St. James Co., 65 F. (2d) 82. Counsel ignores the distinction made by the court that in the St. James case application for the rents was not made until after the rents had been collected. See Appellants' Brief, pp. 20, 21, 25, 33, 67.

Mortgage Loan Co. v. Livingston, 45 F. (2d) 28 (C.C.A. 8). See Appellants' Brief, pp. 21, 23, 64, 66. The significant thing about appellees' discussion of this case (p. 46) is that appellees lay great stress on the supposed fact that "the receiver promptly consented to such segregation" and request by the mortgagee immediately upon institution of the bankruptcy proceedings. In the first place counsel are in error in stating that the receiver consented to application of the rents. All that the receiver consented to was segregation, putting the case on a precise parallel with our case, where there was a court order for the segregation at the outset of the proceedings. Furthermore, counsel's argument that the receiver's consent to segregation (and his supposed consent to application) constitutes a sequestration is in direct negation of counsel's argument concerning claim of Portland Trust & Savings Bank that the trustee in bankruptcy had no right to consent to segregation of the rentals on the Portland Trust properties (Appellees' Brief, pp. 65-7). There counsel argues vigorously that even where the trustee actually deposits the money in a separate trust account, the bankruptcy estate is not bound thereby.

Sullivan v. Rosson, 223 N.Y. 217, 119 N.E. 405. This case has already been discussed by us. See Appellants' Brief, pp. 30, 67. It simply holds that a junior mortgagee is entitled as against a senior mortgagee until such time as the latter takes appropriate action to have the rents applied on the senior mortgage. In recognition of the senior mortgagee's rights, the court says (4 A.L.R., p. 1404):

> "A senior mortgagee desiring to obtain such rents * * * should actually possess himself of them or of the right to them through some mutual arrangement, * * * *or he should make application to the court to have the receivership extended for his benefit* * * *."

We have, in bankruptcy, done the equivalent of the latter.

Re Van Rooy, 21 F. Suppl. 431 (D.C., Ohio). This is a District Court case. The case in no way conflicts with the many cases cited by us. Appellees' own statement of the case is that "**after** the sale of the property" the mortgagee petitioned for segregation covering rents previously collected. The court recognizes that had timely and appropriate application been made by the mortgagee, he would have been entitled to the rents. Appellees quote (p. 25), the court's statement to the effect that the mortgagee, to make the lien effective, should have brought foreclosure proceedings, with the court's consent, or in the alternative should have obtained from the bankruptcy court the appointment of a receiver to collect the rents for the mortgagee's benefit or "at

least it should have made some such attempt". What the court means, obviously, is that the mortgagee did not take timely action to protect his remedy. It may further be noted that in our cases the court ultimately granted leave to foreclose as to all the mortgages, and rents and profits were collected herein after such orders were entered.

In re Wakey, 50 F. (2d) 869 (C.C.A. 7). See Appellants' Brief, pp. 21, 33. The reason that this court refused to follow the *Wakey* case was not, as stated by appellees, that a mortgage creates no lien on future rents. On the contrary, the reason was that the *Wakey* case permits recovery from the date of the bankruptcy proceedings, regardless of the date of application, whereas this circuit limits recovery to the period subsequent to date of application.